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14 UNITED STATES BANKRUPTCY COURT

15 CENTRAL DISTRICT OF CALIFORNIA – SANTA ANA

16 In re

17 THE LITIGATION PRACTICE GROUP P.C.,

18 Debtor.

Case No. 8:23-bk-10571-SC

Chapter 11

19 TRUSTEE’S MOTION TO SURCHARGE
20 PROCEEDS OF SALE SUBJECT TO
21 PURPORTED CLAIMS OF SECURED
22 CREDITORS TO PAY THE SUPER-
23 PRIORITY ADMINISTRATIVE LOANS
24 USED TO FUND OPERATIONS BEFORE
THE SALE CLOSED; MEMORANDUM OF
POINTS AND AUTHORITIES;
DECLARATION OF RICHARD A.
MARSHACK

25 Hearing Date

Date: June 13, 2024

26 Time: 10:00 a.m.

Ctrm: 5C - ViaZoom¹

27 Place: 411 West Fourth Street

Santa Ana, CA 92701

28
¹ Check Judge Clarkson’s tentative calendar prior to hearing for further Zoom instructions.

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1 TO THE HONORABLE SCOTT C. CLARKSON, UNITED STATES BANKRUPTCY COURT
2 JUDGE, THE OFFICE OF THE UNITED STATES TRUSTEE AND ALL INTERESTED
3 PARTIES:

4 Richard A. Marshack, in his capacity as Chapter 11 Trustee (“Trustee”) for the bankruptcy
5 estate (“Estate”) of The Litigation Practice Group P.C. (“Debtor”), respectfully submits this
6 Motion (“Motion”) to Surcharge Secured Proceeds of Sale Subject to Purported Claims of Secured
7 Creditors to Pay the Super-Priority Promissory Notes (“Loans”) Used to Fund Operations Before
8 the Sale Closed, and alleges as follows.

9 **I. Summary of Argument**

10 A court can impose, and a bankruptcy trustee may recover, a section 506(c) surcharge of
11 expenses against secured creditors’ collateral if the trustee can show the expenses were reasonable,
12 necessary, and beneficial to the secured creditors. In this case, the Debtor had fraudulently
13 transferred substantially all its assets prior to bankruptcy, necessitating Trustee’s avoidance and
14 recovery of these assets to prepare them for a subsequent sale, ultimately to the highest bidder
15 Morning Law Group, P.C. (“Buyer”); without this sale, there would likely be no proceeds from
16 which any distributions could be made to secured creditors. Before the Debtor’s assets could be
17 reformed through the sale process and conveyed to a “good faith purchaser” for value, the Debtor
18 had to maintain its going concern value and remain in contact with its clients if there was to be a
19 sale of a going concern business. In a typical case, a debtor operating in chapter 11 typically
20 reaches an agreement with its primary secured creditor for the use of cash collateral to fund
21 operations. This is not a typical case, and the Trustee had no ability to use the Debtor’s cash
22 collateral given that title to and the use of the funds received post-petition were in dispute. To
23 maintain a skeletal operation, the Trustee was forced to borrow money post-petition, with Court
24 authorization (generally “Loans”), to fund limited operations until the completion of a sale. This
25 Motion seeks authority to surcharge the sales proceeds that the Trustee is holding in escrow until
26 the resolution of competing claims of certain creditors to the proceeds are resolved. This will
27 permit the Trustee to repay the Loans on or before they become due in July 2024.

II. Pertinent Factual Background

A. Debtor's Business, Bankruptcy Filing, and Appointment of a Trustee

Pre-petition, Debtor was a law firm that provided consumer debt resolution services and creditor litigation services to clients, servicing more than 50,000 customers across the United States. On March 20, 2023, Debtor filed a voluntary petition under Chapter 11 of Title 11 of the United States Code, initiating bankruptcy Case No. 8:23-bk-10571-SC in the United States Bankruptcy Court for the Central District of California, Santa Ana Division ("Bankruptcy Case"). Prior to bankruptcy, Debtor fraudulently transferred substantially all its assets and clients. As of the petition date, Debtor had virtually no assets or clients.

On March 30, 2023, as Dk. No. 21, the Office of the United States Trustee ("UST") filed a motion to dismiss or convert the Bankruptcy Case under 11 U.S.C. § 1112(b) for failure to comply with its guidelines and requirements for a chapter 11 case. No opposition to the motion was filed.

On May 3, 2023, a hearing was held on the motion to dismiss or convert. At the hearing, the Court directed the UST to appoint a Chapter 11 Trustee. Richard A. Marshack was appointed the Chapter 11 trustee of the Debtor's Estate [Dkt. No. 65].

Upon his appointment, Trustee filed litigation seeking, among other things, to avoid and recover Debtor's fraudulent transfers of its assets and client base. See, Adv. Case No. 8:23-ap-01046-SC. On June 27, 2023, Trustee filed a stipulation with Defendant, Phoenix Law Group, Inc., avoiding, recovering, and preserving the legal service agreements between Debtor and its clients.

B. Loan Proceeds Used For Necessary Expenses Prior to Sale

While the Trustee pursued the recovery of these legal service agreements to have assets to sell, he had to pay those expenses necessary for the Debtor to continue operating to preserve the value of the assets that were to be sold to interested buyers. Because the Trustee could not use the Debtor's cash collateral, the Trustee was forced to borrow money post-petition subject to Court approval. The timeline and history of the Court approved, post-petition financing obtained by the Trustee is set forth in detail on pages 16-18 of the Disclosure Statement filed in support of

1 the Joint Plan of Liquidation [Dkt. No. 1058], and this summary is incorporated herein by
2 reference.

3 The Court approved the Trustee's requests for post-petition borrowing on a final basis in
4 orders entered on or about August 21, 2023 [Dkt. No. 413, 414, and 415]. The Court approved
5 borrowing consisted of four promissory notes with three different lenders although the notes
6 contained substantially the same terms. The details of these notes are below:

- 7 • A promissory note dated on or about July 20, 2023 in the original principal amount of
8 \$249,663.98 bearing interest at eight percent per annum between PanAmerican
9 Consulting, Inc., as lender, and the Debtor, as borrower.
- 10 • A promissory note dated on or about July 1, 2023 in the original principal amount of
11 \$240,000.00 bearing interest at eight percent per annum between Resolution Ventures, as
12 lender, and the Debtor, as borrower.
- 13 • A promissory note dated on or about July 19, 2023 in the original principal amount of
14 \$250,336.02 bearing interest at eight percent per annum between Resolution Ventures, as
15 lender, and the Debtor, as borrower.
- 16 • A promissory note dated July 3, 2023 in the original principal amount of \$550,336.02 less
17 \$9,663.98 that was refunded bearing interest at eight percent per annum between Liberty
18 Acquisitions Group, Inc., as lender and the Debtor, as borrower.

19 These notes require repayment of all accrued and unpaid interest and principal one year from the
20 "Start Date," which is the date of execution. Thus, the estate will be required to repay all amounts
21 owed under these Notes in July 2024.

22 As further detailed in the Declaration of Richard Marshack ("Marshack Declaration")
23 which is attached hereto, which is incorporated herein by reference, the funds obtained from this
24 post-petition borrowing were used to pay and retain the Debtor's employees and pay other
25 necessary expenses until the sale of the Debtor's assets, as reformed, could be completed [See
26 Dkt. No. 249, Exhibit 6 Budget]. Specifically, Paragraphs 10 and 11 of the Declaration, refer to
27 the operating reports filed herein, to show that over one million dollars (\$1,000,000.00) of the
28 borrowed funds were paid either to the Debtor's employees, or on their behalf to third parties like

1 health insurers for post-petition expenses while more than four hundred thousand dollars
2 (\$400,000.00) was paid to the taxing authorities based on these post-petition wages. Furthermore,
3 the Trustee also paid miscellaneous but necessary expenses like (i) charges for employee benefits,
4 (ii) payments to local counsel for clients of the Debtor, and (iii) fees to the Trustee's field agent.
5 (See Declaration at 12). The July 1st Note from Resolution Ventures was deemed satisfied as part
6 of the sale consideration (Declaration ¶ 10). Only three notes remain outstanding.

7 **C. Efforts to Sell Assets and Opposition Thereto**

8 On an accelerated timetable, the Trustee solicited offers for the Debtor's assets and
9 pursued a sale. However, and as set forth in the Declaration, numerous parties opposed the
10 Trustee's sale efforts generally,² and substantial briefing and evidence was necessary to respond
11 to these objections and prove that the Debtor's contracts with consumers could be reformed and
12 sold to a good faith purchaser. (This opposition included a Motion to Convert the Case to One
13 Under Chapter 7 filed by the United States Trustee).³ At the sale hearing, the Court approved the
14 sale over the remaining objections, and on July 22, 2023, the Court entered an order ("Sale
15 Order") granting the Trustee's motion to sell certain assets of the Debtor, as reformed [Dkt. No.
16 320] free and clear of all liens, claims, and encumbrances with same to attach to the proceeds.
17 Pursuant to the Sale Order, the closing happened on August 4, 2023, and the Trustee is presently
18 holding approximately five million dollars (\$5,000,000.00) in sales proceeds ("Proceeds").⁴ (See
19 Declaration ¶ 13). As part of the consideration paid for the Debtor's assets, one note from
20 Resolution Ventures was deemed satisfied, and the Estate is no longer liable under this note.
21 Pursuant to the Asset Purchase Agreement, the Trustee anticipates the buyer will make additional
22 payments based on the income generated from the sold assets as set forth in the Sale Order.

23 As stated above, the Trustee's faced significant opposition in his efforts to sell the
24

25 ² Aside from the objections filed by specific creditors, the docket reflects general objections filed by (i) Carolyn Beech
26 [Dkt. No. 294] which was supported by an amicus brief from the National Consumer Bankruptcy Rights
27 Center filed with leave from the Court [Dkt. No. 288]; (ii) two pleadings in opposition from the United States
Trustee [Dkt. Nos. 259 and 296]; and (iii) an objection from the Unsecured Creditors Committee [Dkt. No.
300].

28 ³ See Motion of the United States Trustee to Convert the Case filed at Dkt. No. 218.

⁴ The Trustee is holding another \$4,697,020.00 in funds seized pursuant to the Temporary Restraining Order entered
in Adversary Proceeding No. 8:23-ap-1046, which funds are frozen pending further order of the Court.

Debtor's assets including a motion to convert the case to Chapter 7. While conversion to chapter 7 would have eliminated the need for post-petition borrowing, it also would have ended any chance of reforming the Debtor's consumer contracts for sale to a good faith purchaser. Without the post-petition financing and payment of necessary expenses to preserve the Debtor's going concern value, there would be no Proceeds for the Debtor's allegedly secured creditors to fight over (See Adv. Pro. No. 8:24-ap-01011 and 8:23-ap-01098). Because every dollar of the Loans benefitted any entity who is determined to hold a valid, perfected security interest in the Debtor's assets by providing time to sell the Debtor's assets, it is appropriate and proper for the Proceeds to be surcharged to pay all amounts owed on the Loans before they mature. Depending on the actual date that the Trustee satisfies the outstanding balance of the Loans, the surcharge of the Proceeds should be no more than \$1,112,762.90.⁵

C. Alleged Secured Creditors

As noted above, there are two adversary proceedings currently pending that have been filed to adjudicate the validity, priority, amount, and extent of the competing and purportedly secured claims to the Proceeds. The Trustee has filed Adversary Proceeding No. 8:24-ap-01011 against several defendants who have asserted a lien on the Proceeds. As of the filing of this Motion, only five defendants – Bridge Funding Cap, LLC; MNS Funding, LLC; Azzure Capital, LLC; Diverse Capital, LLC; and PECC Corp. – in this adversary continue to assert liens against the Proceeds. OHP-CDR, LP and Purchaseco80, LLC have filed Adversary Proceeding No. 8:23-ap-01098 against the Trustee and creditor Azzure Capital, LLC seeking an adjudication of the validity, priority, amount, and extent of their claims to and interests in the Proceeds. The five defendants in Adv. Pro. No. 8:24-ap-01011 and OHP-CDR, LP and Purchaseco80, LLC will collectively be referred to herein as the "Lien Creditors." While the Trustee reserves all rights and claims with respect to the Lien Creditors, the UCC-1 filings of the Lien Creditors are set below:

⁵ This total is comprised of the total of the original principal amounts of the three notes plus the accrual of one year of interest at eight percent per annum (8.0%).

Secured Creditor	UCC Filing Date	UCC Number
Bridge Funding Cap, LLC	5/19/21	U210047914841 ⁶
Azzure Capital LLC	5/28/21	U210050853928
MNS Funding LLC	5/28/21	U210050823723
Diverse Capital LLC	9/15/21	U210085288536
OHP-CDR, LP and Purchaseco80, LLC ⁷	1/25/23	U230005834326
PECC Corp. ⁸	2/2/23	U230009059730

III. Legal Argument

11 U.S.C. § 506(c) provides that a trustee may “surcharge” the collateral of a secured claimant to pay for the reasonable, necessary costs and expenses of preserving or disposing of the collateral:

The trustee may recover from property securing an allowed secured claim the reasonable, necessary costs and expenses of preserving, or disposing of, such property to the extent of any benefit to the holder of such claim.

See also In re Glasply Marine Indus., Inc., 971 F.2d 391, 393 (9th Cir. 1992) (noting that § 506(c) allows a trustee to recover reasonable expense of preserving property to the extent of any benefit to the holder of a secured claim).

Section 506(c) is an exception to the “general bankruptcy rule” that, absent an express agreement to the contrary, the expenses associated with administering a bankruptcy estate are not chargeable to a secured creditor’s collateral or claim, but must be borne out of the unencumbered assets of the estate. 4 COLLIER ON BANKRUPTCY P. 506.05 (2023); *see also U.S.D.A. v. Hopper (In re Colusa Reg’l Med. Ctr.)*, 604 B.R. 839, 853 (B.A.P. 9th Cir. 2019) (noting that § 506(c) codifies an exception to the general rule that bankruptcy administrative expenses may not be charged to or against secured collateral).

⁶ UCC-1 Listed As Being Terminated on 1/2/22 (UCC No. U220114888130). On 1/20/22 Fundura filed a “Lien Statement of Claim” saying debt is still owed and debtor had no right to terminate (UCC No. U220119911529).

⁷ The UCC-1 of OHP-CDR LP was filed in the preference period. Purchaseco80, LLC claims it owns the accounts that it purchased although its ownership would be subject to any valid, prior liens against the Debtor.

⁸ Also recorded in the preference period.

1 Surcharge is not an administrative claim but an assessment against a secured party's
2 collateral. *Debbie Reynolds Hotel & Casino, Inc. v. Calstar Corp. (In re Debbie Reynolds Hotel*
3 *& Casino, Inc.)*, 255 F.3d 1061, 1067 (9th Cir. 2001). A surcharged amount therefore does not
4 come out of the debtor's estate, but rather comes "directly from the secured party's recovery." *Id.*
5 The rationale for charging a lienholder with the costs and expenses of preserving or disposing of
6 secured collateral is that the general estate and unsecured creditors should not bear the cost of
7 "protecting what is not theirs." *Sec. Leasing Partners LP v. ProAlert, LLC (In re ProAlert, LLC)*,
8 314 B.R. 436, 442 (B.A.P. 9th Cir. 2004).

9 Under § 506(c), a trustee may recover administrative expenses from a secured creditor's
10 collateral under § 506(c) if one of two tests is met. *In re Tollenaar Holsteins*, 538 B.R. 830, 833,
11 838 (Bankr. E.D. Cal. 2015). The party seeking surcharge under § 506(c) bears the burden of proof.
12 *In re Colusa Reg'l Med. Ctr.*, 604 B.R. at 853.

13 The first test is an "objective test" which requires that the expenses relating to the
14 preservation or disposition of collateral were:

- 15 1) Reasonable,
- 16 2) Necessary, and
- 17 3) Provided a quantifiable benefit to the secured creditor.

18 *Debbie Reynolds Hotel & Casino, Inc. v. Calstar Corp., Inc. (In re Debbie Reynolds Hotel &*
19 *Casino, Inc.)*, 255 F.3d 1061, 1065 (9th Cir. 2001); *In re Tollenaar Holsteins*, 538 B.R. at 834; *see*
20 *also In re Colusa Reg'l Med. Ctr.*, 604 B.R. at 854 (same). Recovery under the objective test is
21 limited to the amount of any benefit and must be proven with specificity. *In re Tollenaar Holsteins*,
22 538 B.R. at 834. The second test is a "subjective test" under which there must be a showing that
23 the secured creditor "consented to" or "caused" the expenses to be surcharged. *In re Tollenaar*
24 *Holsteins*, 538 B.R. at 834; *see also In re Colusa Reg'l Med. Ctr.*, 604 B.R. at 859 (same).⁹ If the
25 trustee can meet the requirements of either test for surcharge under § 506(c) regarding a particular
26 expense, then the proceeds from the secured party's collateral should be first used to cover the
27 properly surcharged expense instead of being paid to the secured party. 4 COLLIER ON

28 _____
⁹ Absent an agreement, consent shall be deemed pursuant to Local Bankruptcy Rule 9013-1(h).

1 BANKRUPTCY P. 506.05 (2023). Section 506(c), in other words, creates a “special priority” for the
2 surcharged expense ahead of the secured party’s general priority to its collateral. *Id.* Given the
3 obvious objective benefit of the Trustee’s use of the proceeds of the Loans to maintain the value
4 of the Debtor’s assets until the sale closed, the Trustee seeks to surcharge the Proceeds based on
5 the “objective test.”

6 **A. Borrowing Money Through the Loans was Objectively Reasonable,**
7 **Necessary, and Provided a Quantifiable Benefit to the Lien Creditors.**

8 **1. Reasonable**

9 Expenses are reasonable to the extent they are incurred in the ordinary course at a
10 reasonable price. 4 COLLIER ON BANKRUPTCY P. 506.05 (2023). To preserve the Debtor’s going
11 concern value and its relationships with its clients, the Trustee had to retain and pay the wages and
12 benefits of the Debtor’s employees. Because the Trustee could not use the Debtor’s funds or cash
13 collateral on hand, the Trustee had to borrow operating funds via the Loans subject to Court
14 approval. As set forth in the Marshack Declaration, all funds borrowed were used to pay the
15 Debtor’s employees and other necessary and proper expenses related to the Debtor’s post-petition
16 operations. Without these payments, the Debtor would have ceased operations and breached its
17 agreements with its clients. There would be nothing left for a chapter 7 trustee to sell except for
18 office equipment and furnishings. The claims of the Lien Creditors currently exceed the Proceeds.
19 Until the amounts of these claims are fixed and the priority and validity of the alleged security
20 interests adjudicated, the Trustee cannot use the Proceeds to pay the Loans at maturity. It is only
21 fair and proper that the Proceeds be surcharged in the amount of the Loans as this borrowing
22 directly benefited the Lien Creditors. In a chapter 7 case, there would be no Proceeds to fight over.
23 The Lien Creditors also retain their rights to assert liens against additional future consideration
24 paid to the Trustee pursuant to the Sale Order.

25 **2. Necessary**

26 Expenses are necessary where they prevent loss of or diminution in value to property of
27 the estate. *See In re Tollenaar Holsteins*, 538 B.R. 830, 834 (Bankr. E.D. Cal. 2015) (indicating
28 that expenses were necessary to prevent the loss of valuable permits and a corresponding

1 diminution in value if the permits were lost). Expenses are likewise necessary where they secure
2 estate property from vandalism or ensure compliance with regulations. *Id.* at 835 (noting that
3 expenses were reasonable and necessary to secure property from vandalism and comply with
4 environmental monitoring regulations). Importantly, if a secured creditor has a lien on all, or
5 virtually all, of a debtor's assets, the debtor is engaged in ongoing business operations, and the
6 debtor's continued operations preserve or enhance the value of the secured creditor's collateral,
7 items that may qualify as "necessary" expenses chargeable against the collateral include the
8 debtor's payroll costs, insurance costs, workers' compensation expenses, and postpetition
9 administrative taxes. 4 COLLIER ON BANKRUPTCY P 506.05 (16th 2023).

10 The Debtor's business was a law firm that provided consumer debt resolution services to
11 over 50,000 customers across the United States; there were virtually no other significant business
12 assets in the estate other than these consumer client-related accounts.¹⁰ At the October 19, 2023
13 hearing on a prior surcharge motion,¹¹ when discussing the necessity of managing the sale of
14 Debtor's firm, this Court laid out the law of the case, finding that "OHP and other secured creditors
15 wouldn't even have money right now" without Trustee's decisive actions taken in pursuing the
16 sale. There would not even be the current Chapter 11 proceeding and instead, secured creditors
17 would "be talking to a Chapter 7 trustee about how in the world [they are] ever going to get paid."
18 As stated herein and in the Declaration, without the use of the funds obtained from the Loans, the
19 Trustee would not have a going concern business to sell. Because the Trustee used the Loan
20 proceeds to pay employee wages and related expenses and other necessary operating expenses of
21 the Debtor, the repayment of the Loans is a necessary expense of the sale and monetization of the
22 Debtor's assets that should be surcharged to the Proceeds as a direct benefit to the Lien Creditors.

23 **3. Quantifiable Benefit**

24 An estate can be surcharged for expenses that benefit secured creditors and their collateral.
25 *See In re Tollenaar Holsteins*, 538 B.R. 830, 835 (Bankr. E.D. Cal. 2015). Further, the
26

27 ¹⁰ This excludes litigation claims and other causes of action.

28 ¹¹ Trustee's Motion To Surcharge Secured Creditors To Pay Management Fees And Expenses Of Resolution Processing, LLC, Dk. No. 545; Hearing at Dk. No. 597.

1 reasonableness and necessity of a trustee's incurred expenses must be balanced against the benefits
2 obtained for the secured creditor and the amount the secured creditor would have necessarily
3 incurred through foreclosure and disposal of the property. *U.S.D.A. v. Hopper (In re Colusa Reg'l*
4 *Med. Ctr.)*, 604 B.R. 839, 854 (B.A.P. 9th Cir. 2019).

5 Here, the Trustee incurred the Loans in order to fund the Debtor through the closing of a
6 sale. The loan proceeds were used to pay employee wages and related expenses and to pay those
7 certain expenses necessary for the Debtor to remain a going concern. There was total clarity in
8 the record regarding the Loans and the use of the loan proceeds. While the Trustee might be able
9 to satisfy the Loans in the future, the Trustee does not have access to such funds at present and is
10 unlikely to have such funds by July 2024. Currently, the Debtor is obligated to repay the Loans
11 that were used to pay expenses necessary to preserve its going concern value until a sale could be
12 completed. As stated herein and in the Declaration, without the Loans, the Debtor would have
13 gone dark and converted to chapter 7. The Loans are the only reason the Proceeds exist against,
14 and it would be unfair and inequitable for the Lien Creditors to recover from the Proceeds while
15 the Estate is saddled with repayment of the Loans. Given the obvious objective benefit to the Lien
16 Creditors, the Trustee requests that the Proceeds be surcharged pursuant to 11 U.S.C. § 506(c) in
17 an amount sufficient to satisfy the Loans which shall not exceed \$1,134,362.90,

18 **IV. Conclusion**

19 For the foregoing reasons, Trustee requests that the Court enter an order:

- 20 1) Granting the Motion and awarding such other relief as the Court deems proper
21 and appropriate;
- 22 2) Surcharging the Proceeds (without regard to the priority of the Secured
23 Creditors or the allowance of their claims) in an amount necessary to satisfy the Loans, which shall
24 not exceed \$1,112,762.90, representing the total of the principal amount of the Loans plus one year
25 of interest at eight percent per annum;
- 26 3) That such surcharge be without prejudice to any further request for surcharge to be
27 brought by way of separately noticed motion; and
28

1 4) Authorizing Trustee to withdraw sufficient Proceeds from escrow to satisfy the
2 Loans including accrued interest as of the date of payment.

3
4
5 DATED: May 23, 2024

6 DINSMORE & SHOHL LLP

7 By: /s/ Tyler Powellx
8 TYLER POWELL [pro hac vice]
9 CHRISTOPHER CELENTINO
10 YOSINA M. LISSEBECK
11 Special Counsel to Chapter 11 Trustee,
12 RICHARD A. MARSHACK
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Declaration of Richard A. Marshack

I, RICHARD A. MARSHACK, say and declare as follows:

1. I am an individual over 18 years of age and competent to make this Declaration.

If called upon to do so, I could and would competently testify as to the facts set forth in this Declaration.

2. I am the duly appointed Chapter 11 Trustee ("Trustee") of the Bankruptcy Estate ("Estate") of The Litigation Practice Group P.C. ("Debtor").

3. The facts set forth below are true of my personal knowledge.

4. I make this Declaration in support of my Motion ("Motion") for Order to Surcharge Secured Creditors to Pay Super-Priority Administrative Loans Used to Fund Pre-Sale Operations.

5. Prior to bankruptcy, Debtor was a law firm that provided consumer debt resolution services allegedly servicing more than 50,000 customers across the United States.

6. On March 20, 2023, Debtor filed a voluntary petition under Chapter 11 of Title 11 of the United States Code, initiating bankruptcy Case No. 8:23-bk-10571-SC in the United States Bankruptcy Court for the Central District of California, Santa Ana Division ("Bankruptcy Case").

7. On March 30, 2023, as Dk. No. 21, the United States Trustee filed a motion to dismiss or convert the case under 11 U.S.C. § 1112(b) for failure to comply with the U.S. Trustee guidelines and requirements for a chapter 11 case. No opposition to the motion was filed.

8. On May 3, 2023, a hearing was held on the motion to dismiss or convert. At the hearing, the Court directed the U.S. Trustee to appointment a Chapter 11 Trustee in this case. I was appointed as the Chapter 11 trustee of the Debtor's estate.

9. Following appointment as Trustee, my ability to collect, market, and liquidate the assets of the Debtor was limited because (i) the Debtor had improperly transferred many of its consumer engagements to third parties before the bankruptcy and (ii) I had no ability to use the Debtor's cash collateral or funds collected post-petition. Accordingly, I had to borrow money, with the Court approval, to fund the Debtor's limited operations until the assets could be recovered and marketed and a sale could occur. Numerous parties opposed my efforts to sell the Debtor's assets to a good faith purchaser via a chapter 11 sale. Specifically, general objections were filed

1 by (i) Carolyn Beech [Dkt. No. 294] which was supported by an amicus brief from the National
2 Consumer Bankruptcy Rights Center filed with leave from the Court [Dkt. No. 288]; (ii) two
3 pleadings in opposition from the United States Trustee [Dkt. Nos. 259 and 296]; and (iii) an
4 objection from the Unsecured Creditors Committee [Dkt. No. 300]. The United States Trustee
5 also moved to convert the case to Chapter 7 which would have ended any sale efforts. See Dkt.
6 No. 218.

7 10. The Court approved the Estate borrowing funds under four promissory notes with
8 similar terms in three orders entered on or about August 21, 2023 [Dkt. Nos. 413, 414, and 415].
9 One note with Resolution Ventures was deemed satisfied as part of the sale consideration and is
10 no longer payable. Three notes remain outstanding and will be matured and payable in July 2024:
11 the first note is with PanAmerican Consulting, Inc. in the original principal amount of \$249,663.98
12 (“PanAmerican Note”); the second note is with Liberty Acquisitions Group, Inc., in the original
13 principal amount of \$550,336.02 less \$9,663.98 that was refunded (“Liberty Note”); and the third
14 note is with Resolution Ventures in the original principal amount of \$250,336.02. All notes bear
15 interest at eight percent per annum (8.0%) until paid at maturity.

16 11. As shown on the July 2023 Operating Report [Dkt. No. 472-3, Pages 7-31], the
17 estate used the funds advanced pursuant to the Liberty Note to pay employee wages and amounts
18 owed for employee benefits such as insurance. The July cash receipts and disbursement record for
19 the payroll and operating account ending in -4611 shows the receipt of \$500,000.00 pursuant to
20 the Liberty Note on June 30, 2023 followed by the disbursement of almost \$200,000.00 to pay
21 employee wages. Another \$180,000.00 and \$75,000.00 were transferred to the payroll tax account
22 on July 6, 2023 and July 19, 2023 respectively. The estate paid another payroll on July 19, 2023
23 which consumed the remaining funds from the Liberty Note as well as the \$250,336.02 in funds
24 loaned by Resolution Ventures that was deposited on July 19, 2023.

25 12. The proceeds from the PanAmerican Note were deposited on July 20, 2023. Again
26 these funds were immediately used to pay employees and employee related expenses beginning
27 on July 27, 2023. Accordingly, only a little over \$125,000 remained on deposit in this account at
28 the end of July 2023 [Dkt. No. 472-3 Page 31]. The August Cash Receipts and Disbursements

Record for this account is filed in record as part of the August operating report [Dkt. No. 542-3, Page 4]. This operating report shows that \$80,000 of the \$125,000 in funds on deposit at the end of July was transferred to the payroll tax account at the beginning of the month. The remaining \$45,000 or so dollars on deposit was subsequently used to pay additional amounts to employees and for expenses related to operation and preservation of the business (agent fees, insurance, and fees to counsel representing the Debtor's consumer clients). [Dkt No. 542-3, Page 4-13]. The payroll and operating account ended August with a balance of just over nine thousand dollars (\$9,000.00).

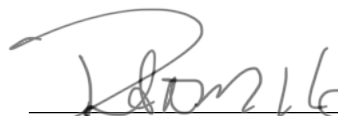
13. On July 22, 2023, as Dk. No. 320, the Court granted Trustee's sale motion of such contracts, as reformed, and entered an order approving the sale of estate assets. The sale was free and clear of all liens, claims, and encumbrances with same to attach to the proceeds of sale ("Proceeds"). Pursuant to the Sale Order, the buyer closed on August 4, 2023. I am currently holding approximately five million dollars (\$5,000,000.00) in escrow in Proceeds. I anticipate additional Proceeds will be received in the future.

14. The use of the borrowed funds directly benefited the secured creditors of the Debtor by providing time for a buyer to be located and for the sale to close. Without this ability to pay employees and keep the Debtor operating, conversion of the case would have been the only option. I therefore request that the Court enter an order surcharging the Proceeds with the payment of the Loans as set forth in the Motion.

15. At this time, the Court has not yet determined the validity, priority, or extent of any of the alleged secured parties' claims. As such, I seek to surcharge the Proceeds. The ultimate determination of which secured creditor will not receive funds as a result of the requested surcharge of the Proceeds will be determined at a later time.

I declare under penalty of perjury that the foregoing is true and correct.

Executed on May 24, 2024.



RICHARD A. MARSHACK

PROOF OF SERVICE OF DOCUMENT

I am over the age of 18 and not a party to this bankruptcy case or adversary proceeding. My business address is:
100 West Main Street, Suite 900, Lexington, KY 40507.

A TRUE AND CORRECT COPY OF THE FOREGOING DOCUMENT ENTITLED: TRUSTEE'S MOTION TO SURCHARGE PROCEEDS OF SALE SUBJECT TO PURPORTED CLAIMS OF SECURED CREDITORS TO PAY THE SUPER-PRIORITY ADMINISTRATIVE LOANS USED TO FUND OPERATIONS BEFORE THE SALE CLOSED; MEMORANDUM OF POINTS AND AUTHORITIES; DECLARATION OF RICHARD A. MARSHACK

will be served or was served **(a)** on the judge in chambers in the form and manner required by LBR 5005-2(d); and **(b)** in the manner stated below:

1. TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING (NEF): Pursuant to controlling General Orders and LBR, the foregoing document will be served by the court via NEF and hyperlink to the document. On **May 23, 2024**, I checked the CM/ECF docket for this bankruptcy case or adversary proceeding and determined that the following persons are on the Electronic Mail Notice List to receive NEF transmission at the email addresses stated below:

☒ Service information continued on attached page

2. SERVED BY UNITED STATES MAIL: On **May 22, 2024**, I served the following persons and/or entities at the last known addresses in this bankruptcy case or adversary proceeding by placing a true and correct copy thereof in a sealed envelope in the United States mail, first class, postage prepaid, and addressed as follows. Listing the judge here constitutes a declaration that mailing to the judge will be completed no later than 24 hours after the document is filed.

PRESIDING JUDGE'S COPY

HONORABLE SCOTT C. CLARKSON
UNITED STATES BANKRUPTCY COURT
411 WEST FOURTH STREET, SUITE 5130 / COURTROOM 5C
SANTA ANA, CA 92701-4593

DEBTOR – MAIL REDIRECTED TO TRUSTEE

THE LITIGATION PRACTICE GROUP P.C.
~~17542 17TH ST, SUITE 100~~
~~TUSTIN, CA 92780-1984~~

☒ Service information continued on attached page

3. SERVED BY PERSONAL DELIVERY, OVERNIGHT MAIL, FACSIMILE TRANSMISSION OR EMAIL: Pursuant to F.R.Civ.P. 5 and/or controlling LBR, on **May 23, 2024**, I served the following persons and/or entities by personal delivery, overnight mail service, or (for those who consented in writing to such service method), by facsimile transmission and/or email as follows. Listing the judge here constitutes a declaration that personal delivery on, or overnight mail to, the judge will be completed no later than 24 hours after the document is filed.

☐ Service information continued on attached page

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct.

May 23, 2024
Date

Tyler Powell
Printed Name

/s/ Tyler Powell
Signature

1. **TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING (NEF):** CONTINUED:

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X-20

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